

Message Text

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ACTION EUR-12

INFO OCT-01 EA-07 ISO-00 CIAE-00 DODE-00 PM-04 H-01 INR-07
L-03 NSAE-00 NSC-05 PA-01 PRS-01 SP-02 SS-15 USIA-06
COME-00 EB-08 LAB-04 SIL-01 TRSE-00 /078 W
-----050402Z 026913 /66

R 041812Z MAR 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC 1262
INFO AMEMBASSY ANKARA
AMEMBASSY ATHENS
AMEMBASSY BERN
AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY CANBERRA
AMEMBASSY COPENHAGEN
AMEMBASSY DUBLIN
AMEMBASSY HELSINKI
AMEMBASSY LISBON
AMEMBASSY LUXEMBOURG
AMEMBASSY MADRID
AMEMBASSY OSLO
AMEMBASSY OTTAWA
AMEMBASSY PARIS
AMEMBASSY REYKJAVIK
AMEMBASSY ROME
AMEMBASSY STOCKHOLM
AMEMBASSY THE HAGUE
AMEMBASSY TOKYO
AMEMBASSY VIENNA
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USMISSION EC BRUSSELS
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C O N F I D E N T I A L SECTION 01 OF 02 LONDON 03719

E.O. 11652: GDS
TAGS: PGOV, PINT' ELAB, EGEN, UK
SUBJECT: BRITAIN IN FEBRUARY: FROM MEDIUM TO WORSE

REF: LONDON 20L4

SUMMARY: FOLLOWING A MIDDLING JANUARY, BRITAIN'S FEBRUARY BEGAN BETTER THAN IT ENDED; EVEN 28 DAYS PROVED TOO MANY. ALTHOUGH THE FINANCIAL SITUATION CONTINUED TO LOOK GOOD, GENERAL ECONOMIC SIGNS WERE LESS FAVORABLE AND PORTENTS FOR THE FUTURE DIMMED. THE OUTLOOK FOR REACHING AN AGREEMENT WITH THE TRADE UNIONS FOR A THIRD YEAR OF EFFECTIVE WAGE RESTRAINT CONTINUED TO GATHER CLOUDS. THE GOVERNMENT'S DEVOLUTION BILL, ITS LEGISLATIVE CENTERPIECE FOR THIS PARLIAMENTARY SESSION, WAS EFFECTIVELY KILLED, IF NOT YET BURIED. IT BECAME CLEARER THAT BRITAIN WOULD HAVE DIFFICULTY ENACTING LEGISLATION FOR DIRECT ELECTIONS TO THE EUROPEAN PARLIAMENT QUICKLY ENOUGH TO MEET THE EC-NINE AGREED TIMETABLE. FOREIGN SECRETARY CROSLAND'S DEATH DEPRIVED GOVERNMENT AND PARTY OF A VALUABLE SENIOR MEMBER; THE LOSS OF THIS MODERATE PILLAR DURING AN ALREADY DIFFICULT PERIOD FOR CALLAGHAN AND COMPANY PROVOKED SOBERING STOCKTAKING AMONG BOTH PRO-GOVERNMENT AND NEUTRAL OBSERVERS. END SUMMARY.

1. MOST BRITONS AND THEIR GOVERNMENT SAW LITTLE CAUSE FOR JOY IN FEBRUARY. TRUE, THE FINANCIAL SECTOR WAS QUIET, WITH THE POUND SHOWING CONSIDERABLE STRENGTH. PRESSURE ON INTEREST RATES WAS DOWNWARD, AND THE STOCK MARKET ROSE. BUT UNDERLYING THIS RARE BRIGHTNESS WAS CONTINUED ECONOMIC STAGNATION, WITH INDUSTRIAL OUTPUT EVIDENTLY GROWING ONLY SLIGHTLY. UNEMPLOYMENT CONTINUES HIGH. IF THERE IS AN ECONOMIC RECOVERY GOING ON, IT CONFIDENTIAL

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IS AN EXTRAORDINARILY SHALLOW ONE, EVEN BY THE LOW BRITISH STANDARD. YET NO ACTUAL DISASTER TROUBLED THE ECONOMIC WATERS DURING FEBRUARY.

2. THERE WAS A PLETHORA OF PORTENTS FOR THE FUTURE, MOST OF THEM GLOOMY. STATISTICS EMERGED THAT SHOWED A HUGE TRADE GAP AND EXCEPTIONALLY HIGH RISES IN BOTH THE RETAIL AND WHOLESALE PRICE INDICES FOR JANUARY. THE RATE OF INFLATION IS AT LEAST TEMPORARILY ON THE UPSWING AND IS NOW RUNNING ABOVE 16 PERCENT. COUPLED WITH NEW EARNINGS DATA, THE CONCLUSION IS CLEAR THAT REAL INCOME FELL IN 1976 AND WILL CONTINUE TO DECLINE AT LEAST FOR THE REMAINDER OF THE CURRENT SECOND ROUND OF WAGE POLICY.

3. THE SURPRISINGLY BELATED REALIZATION OF THIS DROP IS MAKING THE NEGOTIATIONS FOR A THIRD YEAR OF PAY RESTRAINT, TO BEGIN AUGUST 1, ALL THE MORE DIFFICULT. THERE IS NOW A LULL IN THESE NEGOTIATIONS; IN MID-MONTH

THE TUC MADE IT CLEAR THAT SERIOUS NEGOTIATIONS CAN ONLY BEGIN AFTER THE CHANCELLOR REVEALS HIS TAX-CUTTING HAND IN THE BUDGET DUE ON MARCH 29.

4. WHILE A THIRD ROUND ACCORD OF SOME SORT REMAINS PROBABLE, REACHING AGREEMENT ON A POLICY THAT WILL MEANINGFULLY RESTRAIN WAGE INCREASES WILL BE DIFFICULT. MOREOVER, A SMALL BUT GROWING MINORITY IS ASKING WHETHER IT WOULD NOT BE BETTER TO ABANDON THE QUEST. THIS MINORITY CAN POINT TO THE BAD EFFECTS OF THE EXISTING PAY POLICY, WHICH HAS COMPRESSED DIFFERENTIALS AND MADE IT IMPOSSIBLE TO RESOLVE ANOMALIES. SUCH

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PROBLEMS -- ALONG WITH OTHERS -- COULD BE VIVIDLY SEEN
IN THE UNOFFICIAL STRIKE OF TOOLMAKERS, WHICH AT THE
END OF FEBRUARY WAS CRIPPLING BRITISH LEYLAND'S
AUTOMOBILE OUTPUT AND CALLING INTO QUESTION THE SURVIVAL
OF THAT MAJOR FIRM.

5. THE GOVERNMENT SLOGGED ALONG WITH ITS DEVOLUTION
BILL THROUGH MOST OF FEBRUARY WHILE TRYING TO BUILD
SUPPORT FOR AN ALL-IMPORTANT TIMETABLE MOTION TO LIMIT
DEBATE. IT OVERWHELMINGLY WON THE BATTLE TO GET
PARLIAMENT TO ENDORSE THE PRINCIPLE OF HOLDING
REFERENDA IN SCOTLAND AND WALES. THEN IT RESOUNDINGLY
LOST THE WAR TO INVOKE CLOTURE WHEN TOO MANY LABOR
REBELS RESISTED POWERFUL PRESSURES TO BRING THEM INTO
LINE AND LIBERAL AND CONSERVATIVE DEVOLUTIONISTS
ABANDONED THE BILL. ALTHOUGH THE GOVERNMENT THEREUPON
BEGAN BILATERAL TALKS WITH ALL OTHER PARTIES,
OSTENSIBLY TO SEE HOW TO MODIFY AND SAVE THE BILL, ITS
DEATH HAS BEEN BROADLY CERTIFIED. THE GOVERNMENT'S
REAL CONCERN IS TO LIMIT POLITICAL DAMAGE CAUSED BY
THE DEVOLUTION DEBACLE.

6. THE TIME THAT PARLIAMENT WILL NOW NOT SPEND ON THE
DEVOLUTION BILL COULD PRESUMABLY BE DEVOTED TO ENACTING
LEGISLATION TO INSTITUTE DIRECT ELECTIONS TO THE
EUROPEAN PARLIAMENT. BUT THAT'S AN EVEN LESS POPULAR
CAUSE WITHIN THE LABOR PARTY THAN DEVOLUTION. DESPITE
HMG'S COMMITMENT TO ITS EC PARTNERS TO USE ITS BEST
ENDEAVORS TO ENACT LEGISLATION IN TIME TO PERMIT
ELECTIONS BY MAY OR JUNE 1978, DURING A MEETING AT
MONTH'S END THE BRITISH CABINET SHOWED ITSELF DEEPLY
DIVIDED ON THIS THORNY QUESTION. WITH MORE DELAY IN
SIGHT, THE ODDS LENGTHENED AGAINST BRITAIN'S
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MEETING THE DEADLINE.

7. FOREIGN SECRETARY CROSLAND WAS FELLED BY A STROKE IN MID-MONTH. PRIME MINISTER CALLAGHAN SURPRISED MOST OBSERVERS BY BOLDLY NAMING CROSLAND'S 38-YEAR-OLD DEPUTY, DR. DAVID OWEN, TO SUCCEED HIM. A NUMBER OF PRACTICAL REASONS CONVERGED TO MAKE OWEN'S NOMINATION THE SENSIBLE ONE. THESE INCLUDED THE UNTIMELINESS OF MOVING THE LOGICAL NOMINEE, CHANCELLOR OF THE EXCHEQUER DENIS HEALEY, FROM THE TREASURY, AS WELL AS THE NEED TO HAVE A FOREIGN SECRETARY WHO COULD AT ONCE EFFECTIVELY CHAIR THE EC COUNCIL OF MINISTERS THROUGH THE END OF JUNE. OWEN'S EARLIER PERFORMANCE HAD DEMONSTRATED TO CALLAGHAN HE COULD HANDLE THE JOB, AND THE PRIME MINISTER ALSO SAW ADVANTAGE IN COLORING THE CABINET'S GRAYING IMAGE WITH SOME REDDER YOUNG BLOOD. CROSLAND'S DEMISE, NEVERTHELESS, SHORTLY AFTER ROY JENKINS' DEPARTURE FOR BRUSSELS, WAS AN ESPECIALLY HURTFUL LOSS FOR THE PARTY AND GOVERNMENT. HIS PASSING MARKED THE DISAPPEARANCE OF A HIGHLY RESPECTED THINKER -- A FAIRLY RARE BIRD AMONG LABOR'S SENIOR MODERATES.

8. WHEN THE CONSERVATIVES EASILY WON A BY-ELECTION TO RETAIN THE SAFE SEAT GIVEN UP BY NEW EC COMMISSIONER CHRISTOPHER TUGENDHAT, THE COMBINED OPPOSITION MOVED INTO A MAJORITY OF ONE OVER LABOR AND ITS REGULAR ALLIES IN THE HOUSE OF COMMONS. THE CONSERVATIVES, MOREOVER, HAVE A GOOD CHANCE OF WINNING CROSLAND'S MARGINAL SEAT AND EVEN AN OUTSIDE ONE OF CAPTURING JENKINS' OLD CONSTITUENCY, THUS FURTHER REDUCING THE 32-SEAT GAP BETWEEN THEM AND THE GOVERNING LABOR PARTY.

9. WITH PARLIAMENTARY ARITHMETIC WORSENING, THE ECONOMIC SITUATION STILL DAUNTING, AND AN UNDIGESTED DEFEAT IN THEIR DEVOLUTION FIGHT, CALLAGHAN & CO. ARE CONFIDENTIAL

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HAVING ONE OF THEIR MANY BAD MOMENTS. BUT WITH NOTHING IN SIGHT WHICH LOOKS AS THOUGH IT COULD UNITE THE OPPOSITION ON ANY CONFIDENCE ISSUE, THE PROSPECT FOR THE FORESEEABLE FUTURE IS THAT THE GOVERNMENT WILL ENTER A HOLDING PATTERN, BUT BE LEFT WITH THE PLEASURES OF POWER.

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC CONDITIONS, ECONOMIC REPORTS
Control Number: n/a
Copy: SINGLE
Sent Date: 04-Mar-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977LONDON03719
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Expiration:
Film Number: D770076-0220
Format: TEL
From: LONDON
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770393/aaaadvx.tel
Line Count: 277
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 20c1adbd-c288-dd11-92da-001cc4696bcc
Office: ACTION EUR
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 6
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: 77 LONDON 20
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 15-Nov-2004 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 3209038
Secure: OPEN
Status: NATIVE
Subject: BRITAIN IN FEBRUARY: FROM MEDIUM TO WORSE
TAGS: PGOV, PINT, ELAB, EGEN, UK
To: STATE
Type: TE
vdkgvwkey: odbc://SAS/SAS.dbo.SAS_Docs/20c1adbd-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009